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SUBJECT: Sri Lanka: The political importance of signing an FTA for the GSL and the peace process

Refs: (A) Colombo 1808 (D) Colombo 1686  
- (B) Colombo 1702 (E) Colombo 1673  
- (C) Colombo 1689

(U) Classified by Ambassador Jeffrey J. Lunstead.  
Reasons 1.5 (b,d).

1. (C) SUMMARY: Mission has reviewed the key economic issues involved in possibly signing a Free Trade Agreement with Sri Lanka in Reftels. In this message, Mission sketches out the domestic political context. In a nutshell, the GSL, deeply worried about maintaining support for the peace process in the south, is selling peace as vital for jobs and economic growth, and an FTA as an important factor in providing such benefits. Conversely, however, the GSL is worried that not signing an FTA could undermine public confidence that the peace process will bring real prosperity. The GSL concerns have a real foundation: with the expiration of the Multi-Fiber Agreement (MFA) in 2005, thousands of jobs are projected to disappear, and an FTA could play a role in preventing that from occurring. We think the GSL's argument that an FTA can play a role in realizing economic gains and thus help the peace process -- the success of which is the USG's number one goal in Sri Lanka -- is one that has considerable merit. END SUMMARY.

2. (C) In Reftels, Mission has reviewed in detail the key economic issues involved in possibly signing a Free Trade Agreement with the Sri Lankan government. In this message, Mission sketches out the domestic political context.

3. (C) In a nutshell, the GSL, deeply worried about maintaining public support for the peace process in the south, is emphasizing that peace will lead to increased economic growth and jobs. In making this point, the GSL sees a possible FTA as important in ensuring such benefits. Regarding the situation in the south, the Prime Minister and his ministers underscore to Mission staff all the time the point that the peace process cannot work unless the Sinhalese Buddhist majority remains on board. Thus far, based on polling and what we hear anecdotally, the peace process has proven extremely popular among all of Sri Lanka's ethnic communities, including the Sinhalese Buddhists. The GSL, however, is worried that the many bumps in the way of getting to a possible final settlement, which mostly involve dealing with the difficult Tamil Tigers and a tense cohabitation situation, could eventually unhinge public opinion in the south.

4. (C) In light of this deep concern, the government -- in a concerted effort to maintain public support in the south -- is relentlessly hammering home the point that the peace process means increased jobs and economic growth for Sri Lanka. Prime Minister Ranil Wickremesinghe, and G.L. Peiris and Milinda Moragoda, two highly sophisticated ministers, as well as more grassroots politicians in the PM's party, directly emphasize in nearly every speech they make that peace and prosperity are inextricably linked. As part of this argument, the point is often made that an FTA with the U.S. would enhance the peace dividend. Given the economic importance attached to reaching an FTA by the government, the proposal has become of interest to the public, which, we believe, sees the fact that the idea is even being taken seriously by the U.S. as a natural benefit flowing from peace.

5. (C) Conversely, however, the government is worried that the ramifications of not attaining an FTA would be severe for the economy and thus for its peace process policies. In essence, the government fears that jobs will be lost without an FTA, and, due to this, the public will become disgruntled about the economic situation and take its anger out on the peace process.

It will also be seen, they fear, as disproving the PM's thesis that the international community, and especially the U.S., will support Sri Lanka's peace process with deeds as well as words. The ultimate concern is that a serious letdown on the economic front could lead to protests against the peace process and instability across the south. This is not an idle concern: many previous efforts to attain peace in Sri Lanka have been wrecked or severely undercut by protests in the south.

16. (C) We think the broad outlines of the GSL's argument described above have a solid foundation. The expiration of the MFA in January 2005 is correctly seen as a hugely important economic event in Sri Lanka, with five percent of the workforce potentially negatively affected. While there have been commendable efforts towards vertical integration of the garment sector, and a move toward consolidation into the high-end garment area, the GSL still views an FTA as a must for preserving market access to the U.S., which buys over 60 percent of the country's garment exports. Most senior GSL officials recognize that an FTA is not a panacea, and recognize that rule-of-origin constraints, particularly with regard to textiles, will be a key challenge. Nonetheless, the increased opportunities for market access provided by an FTA, particularly as Sri Lanka consolidates the garment industry and works to diversify its export base, is seen to be an offset to the potential loss of jobs projected as a result of the MFA expiration. Essentially, if an FTA is signed, at the end of the day the GSL can argue that it was due to international confidence in the peace process that jobs were saved.

17. (C) COMMENT: In addition to the domestic political angle and as reviewed in Reftels, the GSL's pursuit of an FTA with the U.S. has a core substantive policy aspect involving its support for trade liberalization designed to enhance Sri Lanka's reputation as a regional trading hub. The GSL supported U.S. positions in Cancun, continues to be a voice of reason in multilateral trade fora, and has embraced the view that global trade liberalization is necessary for its future economic well-being. All that said, the government's political concerns described above are imperatives that are playing a key role in its strongly pro-FTA position. In Mission's estimation, the GSL's argument that an FTA can play a role in realizing economic gains and thus help the peace process -- the success of which is the USG's number one goal in Sri Lanka -- is one that has considerable merit. END COMMENT.

18. (U) Minimize considered.

LUNSTEAD